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SUBJECT: EGYPTIAN COURT BLAMES FIRMS FOR CEMENT INFLATION

REF: A) CAIRO 396
B) CAIRO 1352

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¶1. (SBU) SUMMARY: A Cairo court fined 20 cement executives including Amcham President Omar Mohanna USD \$1.9 million each for collusion to fix cement prices, blaming the companies for contributing to soaring inflation and in particular the rising cost of much-needed housing. While Trade Minister Rachid Rachid claimed the convictions would encourage more competition and transparency in the market, business leaders said it was another worrying indication of the government making the private sector a scapegoat for its political woes. END SUMMARY.

¶2. (U) A Cairo court fined 20 cement executives 10 million Egyptian pounds (\$1.9 million) each, personally, and their companies another 10 million pounds (\$1.9 million) each on August 25 for conspiring to increase cement prices. The Ministry of Trade and Industry had accused the companies and executives of anti-competitive practices in October 2007 after a 14-month investigation by the ministry's Egyptian Competition Authority (ECA). Among the convicted companies are Suez Cement, Egypt's largest cement producer, as well as Misr Beni Suef Cement, Misr Qena Cement, and Tora Cement.

¶3. (SBU) The Sinai Cement managing director told us previously that soaring demand is responsible for the increased prices, arguing that collusion to fix prices would only make sense when demand is low (ref A). He noted that the period in which the companies are accused of colluding coincided with the start of Egypt's construction boom.

¶4. (SBU) Omar Mohanna, president of the American Chamber of Commerce in Egypt and chairman of Suez Cement, told the press that the executives and companies would be exonerated on appeal, now scheduled to be heard Nov. 4. Privately, he had shrugged off the charges as politically motivated and a cost of doing business in Egypt, and indeed the fines pale in comparison to recent profits. Suez Cement reported a 29-percent increase in profits in the first half of 2008 to LE 768.99 million (\$145 million).

¶5. (U) The trial is the first under Egypt's three-year-old anti-monopoly law designed to bring Egyptian competition policy into line with international practice, efforts supported by USAID. The GOE amended the law in June 2008 to increase maximum fines 10-fold to LE 100 million (\$19 million).

¶6. (SBU) Minister of Trade and Industry Rachid Mohamed Rachid said in a press statement that the ruling would not only protect customers but also enhance the investment climate by increasing competition. In response to public criticism of rising cement prices, Rachid levied an export duty on cement in February 2007 and a ban on cement exports altogether in March 2008. Prices have since fallen to LE 485 per ton from their peak of LE 550 a ton earlier this year. (Comment: Many Egyptians track the politically sensitive price of cement. Just as subsidized bread prices are a barometer of the government's commitment to the poor, cement prices indicate to average Egyptians their ability to get ahead by building, or expanding, homes for themselves and their extended family. End comment.)

¶7. (U) Meanwhile, steel prices have nearly doubled since last year, and the competition authority is investigating Egypt's steel sector, dominated by senior ruling National Democratic Party official Ahmed Ezz. According to press accounts, the results of the steel investigation will be announced in September. Higher steel as well as cement prices have contributed to an inflation rate that hit 22 percent year-on-year in July.

¶8. (SBU) An EFG Hermes analyst told us that in the case of steel, rising costs for raw materials -- rather than illegal price collusion -- appear to be responsible for rising prices. The explanation for rising cement prices is less clear, however. Analysts think the cement price increase was primarily the result of increased demand and hoarding by wholesalers. In addition, in an oligopoly like the cement industry, the small number of producers that dominate the market are often able to follow a similar pricing strategy. Some speculate that cement producers agreed among themselves to export surplus production and not compete for domestic market share. Regardless, it is clear that cement profits increased as prices rose while costs remained low.

¶9. (SBU) Comment: Egypt has a tradition of collusion among the cozy class of industrialists and government officials. Thus, we welcomed the passage of the anti-monopoly law and the creation of the Competition Authority as an important part of Egypt's development from a planned economy to one which supports market practices and private sector development, but which regulates private sector responsibly. As a first test of the new law, the Competition Authority has taken on some of Egypt's wealthiest and most powerful industrialists. Proving price fixing and monopolistic behavior is difficult in any country, and as revealed by this first test, the capacity of the authority is unclear. The argument that the prices are rising as a result of increasing demand and regulatory burdens that limit supply, rather than anti-competitive business practices, is compelling, although without seeing the evidence which has been presented, we do not know the actual degree of price fixing taking place. The ECA began and finished its analysis before the current round of high inflation hit, but as the government comes under fire for not adequately controlling prices (as was routinely expected in years gone by), it is possible that this court decision may have been rendered for political reasons to satisfy the frustrated masses. Rather than encourage investment, this case -- like the recent troubles of Canadian chemical company Agrium (ref B) -- may discourage the investment that Egypt needs to create jobs and continue its recent trend of solid economic growth.

SCOB EY